

July 13, 2006

*Michael C. Schlachter, CFA
Managing Director*

Mr. Russell Read
Chief Investment Officer
California Public Employees' Retirement System
400 Q Street
Sacramento, CA 95814

Re: International Fixed Income Spring Fed Pool Recommendation

Dear Russell,

You had requested Wilshire's opinion with respect to Staff's recommendation of candidates for the Non-US Fixed Income mandate to be included in CalPERS' Spring-Fed Pool. Wilshire concurs with Staff's recommendation.

Background

Staff released a Request for Proposal (RFP) for Non-US Fixed Income managers. CalPERS received 17 useable responses for the mandate¹.

Staff is recommending the following managers for addition to the Spring-Fed Pool:

AllianceBernstein L.P.
BlackRock Financial Management, Inc.
Brandywine Asset Management, LLC
Mondrian Investment Partners Limited
Morgan Stanley Investment Management
Pacific Investment Management Company (PIMCO)

Discussion

Wilshire independently reviewed and evaluated all of the candidates who responded to CalPERS' RFP. Our process has consisted of several steps:

- A qualitative assessment of a firm's organizational and ownership structure, quality and caliber of professional staff, depth of resources, pending litigation, compliance, and culture.

¹ Wilshire's Disclosure of Conflicts of Interest in regard to the managers who responded to the RFP is attached to this agenda item as an appendix.

- A qualitative assessment of a firm's investment process that addresses the sources of information the firm uses to start its investment process, its uniqueness and processing; its ability to use that information or research to forecast the expected results of its individual investments; the process by which portfolios are constructed, including risk management and alpha generating considerations; the firm's ability to implement, including its resources dedicated to trading; and performance attribution: how the firm reviews its results and utilizes the attribution as a feedback mechanism to address performance and risk issues early on, and to communicate results to clients.
- Additionally, Wilshire also conducts several quantitative assessments, including its own detailed attribution analysis and a calculation and assessment of product characteristics, which, for non-US fixed income, includes country and currency allocations, interest rate movement and duration exposure, and credit risk exposure.

Wilshire also participated in Staff's interviews of the candidates that took place in each manager's office in either London, New York City, or the Los Angeles area. Staff has received copies of Wilshire's analyses and qualitative assessments of all the candidates.

Findings and Recommendations

Wilshire has determined that each of the candidates that Staff is recommending for the pool of candidates are solidly of institutional quality, and are highly evaluated by Wilshire. Further, Wilshire also reviewed the proposed "fit" of each candidate against Staff's stated objectives for this search, namely to identify manager products that can further CalPERS' goal of consistent out-performance within a well-managed risk framework. The managers Staff is recommending offer products that are consistent with these objectives.

Given that domestic Fixed Income is largely managed by internal Staff, each manager was also queried as to how it can join CalPERS in a strategic relationship that can contribute to the performance of the overall Fixed Income portfolio. We are satisfied that the managers recommended by Staff will be able to contribute significantly to the overall investment success of the Fixed Income portfolio.

Wilshire reviewed the firms that Staff did not select to determine if there were any products proposed that should have been included. Wilshire is satisfied that Staff has not excluded any firms that should have been included. Although Wilshire believes that there are "Global" managers (i.e., those whose portfolios would include both US and non-US Fixed Income investments) that were on par with the recommended managers, none of these were able to provide sufficient information regarding their abilities in managing purely non-US portfolios, and could not prove whether the value-added in their global portfolios came from non-US management, US management, or dynamic allocations between the US and non-US regions. If such managers had been hired for Global Fixed Income portfolios, Staff would have needed to reduce the size of the US

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Fixed Income portfolio managed internally to maintain the US/non-US balance. As a result, Global managers were excluded from consideration.

Wilshire recommends that the Investment Committee approve the list of managers Staff is requesting to be included in the Spring-Fed Pool of Non-US Fixed Income managers.

Staff will bring recommended policy changes for the externally managed non-US Fixed Income policy to the Policy Sub-Committee in October, and Wilshire anticipates reviewing and commenting on Staff's recommended changes.

Should you require anything further or have any questions, please do not hesitate to contact us.

Sincerely,

A handwritten signature in black ink, appearing to read "Michael Schlachter", with a long horizontal flourish extending to the right.

Michael C. Schlachter, CFA